

## **LBNL - PROCUREMENT STANDARD PRACTICES**

**Section: 49 Termination of Subcontracts**

**Subject: 49.1 Termination for Convenience**

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**PURPOSE:** This standard practice (SP) describes the Laboratory's policy and establishes procedures for the termination of subcontracts for convenience.

**POLICY:** The Laboratory reserves the right to terminate subcontracts completely or partially, even though subcontract performance is satisfactory, when the decision to do so is in the best interest of the Laboratory or the government. For example, termination for convenience may be necessary when a program's requirements are changed or canceled or there is a reduction in or lack of funds.

**SCOPE:** This SP applies to all terminations for convenience except for subcontracts for commercial items. (See SP 2.1, *Definitions of Words and Terms -- General*, for definition of commercial item.)

### **DEFINITIONS:**

**Notice of Termination** Notice of Termination is the formal written termination of the subcontractor's right to proceed further under a subcontract.

**Plant Clearance Period** Plant clearance period is the period beginning on the effective date of the termination and ending 90 days after receipt by the procurement specialist of acceptable disposition schedules for the termination inventory. The 90-day period may be extended by agreement between the Laboratory and the subcontractor.

**Settlement Proposal** Settlement proposal is a proposal for effecting settlement of a subcontract terminated in whole or part that is submitted by the subcontractor to the procurement specialist. The proposal must contain all cost elements, in reasonable detail, supported by adequate accounting data, including settlements with lower-tier subcontractors and any proposed profit.

**Termination for Convenience** Termination for convenience is the exercise of the Laboratory's contractual right to terminate a subcontract when it is in the Laboratory's or the government's best interest to do so.

**Termination Inventory** Termination inventory includes metals, raw materials, and purchased parts the subcontractor obtained for performance of the subcontract. Termination inventory also includes special tooling, special test equipment, government-furnished property, finished components, and work-in-process materials that were somehow altered by the subcontractor in performance of the subcontract.

### **PROCEDURES:**

**OCI** A subcontract may be terminated for convenience if it becomes apparent that an organizational conflict of interest (OCI) exists

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and for reasons other than avoidance of performance of work, the subcontractor cannot or chooses not to mitigate the OCI problem. (See SP 9.3, *Organizational Conflicts of Interest*.)

### **Concurrence**

The concurrence of the Procurement Manager must be obtained before any formal action is taken to terminate a subcontractor.

### **Urgency**

Usually initiated by the requesting organization, terminations must be handled quickly; costs continue to accrue each day the work continues although a requirement no longer exists. It is usually not advisable to forewarn subcontractors of an impending termination as this may encourage the subcontractor to increase its costs.

### **Notice of Termination**

Upon determination that a subcontract is to be terminated for convenience, a written Notice of Termination should be sent promptly to the subcontractor. The notice must state:

- That the subcontract is being terminated for the convenience of the Laboratory under the subcontract clause authorizing the termination;
- The effective date of termination;
- The extent of termination, e.g., partial or whole (if partial, a specific description of the portions of the scope of work that are terminated and not terminated);
- Any special instructions;
- The steps the subcontractor should take to mitigate the impact on subcontractor personnel, if the termination results in a significant reduction in the subcontractor's work force; and
- That the subcontractor is to submit a settlement proposal within a specified number of days from receipt of the Notice of Termination.

### **No-Cost Settlement**

A no-cost termination settlement should be negotiated when:

- The subcontractor has not incurred costs for the terminated portion of the subcontract and
- There are no outstanding payments for damages or other subcontractor obligations due to the Laboratory.

In certain situations, a cancellation or no-cost, no-obligation agreement may be effected rather than a Notice of Termination.

### **Subcontractor Obligations**

The subcontractor must fulfill the following obligations, regardless of any pending subcontract adjustments or settlements.

- Stop Work — Stop work immediately on the terminated portion of the subcontract but complete performance of work not

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terminated; advise the Laboratory of any special circumstances precluding the stoppage of work.

- **Lower-Tier Subcontracts** — Place no further lower-tier subcontracts or orders except as necessary to complete the continued portion of the subcontract, if any; terminate all lower-tier subcontracts to the extent that they relate to the work terminated; and, if directed by the Laboratory, settle all outstanding liabilities and termination settlement proposals arising from the termination of lower-tier subcontracts.
- **Laboratory Assignment** — If directed by the Laboratory, assign to the Laboratory all right, title, and interest of the subcontractor under the terminated lower-tier subcontracts. In this case, the Laboratory is responsible for settlement of the lower-tier subcontractors' termination proposals.
- **Property** — Protect, preserve, and deliver to the Laboratory all government-furnished or subcontractor-acquired property in which the Laboratory has or may acquire an interest. Termination inventory must be disposed of at the direction or authorization of the Laboratory.
- **Settlement Proposal** — Promptly submit a settlement proposal, with appropriate supporting data, for the terminated portion of the subcontract and any accepted material not previously paid for by the Laboratory and a request for subcontract price adjustment for any continued portion, if the termination is partial. The settlement proposal must cover all cost elements including settlements with lower-tier subcontractors and any proposed profit.

### **Disposal of Termination Inventory**

The subcontractor must use its best efforts to sell the termination inventory during the plant clearance period at prices authorized by the Laboratory and without extending credit to purchasers (see SP 45.1, *Government Property*). If inventory remains after the plant clearance period, the government assumes responsibility for the property (by accepting title in the case of a fixed-price subcontract) and must incur the expense of storing, removing, or disposing of the termination inventory within 90 days.

The proceeds of any property transfer or sale of termination inventory must be applied to reduce the Laboratory's payments to the subcontractor, credited to the cost or price of the work, or paid in any other manner as directed by the Laboratory.

### **Settlement Proposals**

The subcontractor must submit a final termination settlement proposal, within one year from the termination date (unless extended in writing), in an acceptable format and supported by

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accounting data and other information sufficient for adequate review by the Laboratory.

There are generally two acceptable bases for termination settlement proposals: "inventory" and "total cost."

**Inventory Basis** — Use of the inventory basis for settlement proposals is preferred. Under this basis, the subcontractor may propose only costs allocated to the terminated portion of the subcontract, and the settlement proposal must itemize the following items separately:

- Metals, raw materials, purchased parts, work in process, finished parts, components, dies, jigs, fixtures, and tooling at purchase or manufacturing cost;
- Charges, such as engineering costs, initial costs, and general administrative costs;
- Costs of settlements with lower-tier subcontractors;
- Settlement expenses; and
- Other proper charges.

An allowance for profit or adjustment for loss must be made to complete the total settlement proposal. All unliquidated advance and progress payments and all disposal and other credits known when the proposal is submitted must then be deducted.

**Total Cost Basis** — When use of the inventory basis is not practicable or will unduly delay settlement, the total cost basis may be used, if approved in advance by the Laboratory, as in the following examples:

- If production has not commenced and the accumulated costs represent planning and preproduction or "get ready" expenses;
- If, under the subcontractor's accounting system, unit costs for work in process and finished products cannot readily be established;
- If the subcontract does not specify unit prices; or
- If the termination is complete and involves a letter subcontract.

The subcontract price for all end items delivered or to be delivered and accepted must be deducted. All unliquidated advance and progress payments and disposal and other credits known when the proposal is submitted must also be deducted.

### **Allowable Settlement Costs**

Settlement proposals are subject to the requirements for certified cost or pricing data. (See SP 15.6, *Cost or Price Analysis*.)

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The Laboratory may be liable to the subcontractor for full compensation for performance up to the date of termination. A reasonable amount for undelivered or unaccepted portions of the terminated subcontract may also be allowable. In determining the reasonable amount, the inventory or total cost basis should be used. In many cases, the cost of termination inventory will be based upon estimates. If the estimates prove difficult to verify, the subcontractor should include a reasonable justification in the settlement proposal. Reasonable costs of preparing the settlement proposal and settling the terminated work are also allowed.

If the subcontractor fails to submit a settlement proposal within the time allowed, the Laboratory may issue a unilateral decision regarding the amount of allowable settlement costs, based upon the available information.

### **Profit**

Profit is allowed on subcontracts terminated for convenience. The procurement specialist must negotiate a fair and reasonable profit for preparations made and work done on the terminated portion of the subcontract. The requesting organization can help evaluate the complexity of work and assist in the determination of a fair profit. A subcontractor's efficiency, economy, cost consciousness, risk, and inventiveness should be considered when negotiating a profit or award fee. Because incurred costs are not always an accurate indication of percentage of subcontract completion or of the true effort expended by the subcontractor, the final termination settlement proposal must be negotiated with the understanding that cost overruns or underruns can create distortion.

### **Unallowable Settlement Costs**

Payment for the loss of anticipatory profits (i.e., the profit that would have been made on the terminated portion had the subcontract not been terminated), consequential damages, interest, or profit on settlement expenses are not allowed.

### **Subcontractor's Appeal**

Under the *Disputes* clause of the subcontract, the subcontractor may appeal any decision made by the Laboratory, except the Laboratory's unilateral determination of settlement costs if the subcontractor fails to file a timely settlement proposal.

### **Restriction**

Under no circumstances will the settlement amount exceed the original subcontract price.

### **Settlement Agreement**

A modification to the subcontract must be executed to reflect the settlement proposal agreement.

## **REVIEWS/APPROVALS:**

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**Laboratory Counsel**

When deemed appropriate, review and advice on termination activities may be sought from Laboratory Counsel.

**Procurement  
Manager**

Before any formal action is taken to proceed with the termination, the concurrence of the Procurement Manager must be obtained.

### **RESPONSIBILITIES:**

**Procurement  
Specialist**

The procurement specialist must:

- Obtain concurrence from the Procurement Manager before taking formal action to terminate a subcontractor for convenience;
- Issue a written Notice of Termination to a subcontractor promptly upon determination that a subcontract is to be terminated;
- Ensure that the subcontractor fulfills its remaining contractual obligations regardless of any pending adjustments or settlements;
- Closely monitor the settlement proposal agreements of lower-tier subcontracts whether negotiated by the subcontractor or the Laboratory;
- Closely monitor the sale or transfer of termination inventory by the subcontractor and delivery of government-furnished or subcontractor-acquired government property to the Laboratory;
- Modify the subcontract to process the final settlement;
- Obtain Laboratory Counsel advice and review of termination for convenience, if needed; and
- Negotiate a fair and prompt settlement with the subcontractor.